

## **Chapter 165**

### **Prudential Standards for Domestic Risk Retention Groups**

#### **Contents**

- Section 1. Authority and Purpose
- Section 2. Scope
- Section 3. Licensure
- Section 4. Corporate Governance and Operational Standards for Domestic RRGs
- Section 5. RRGs Licensed as Captive Insurers
- Section 6. Severability
- Section 7. Effective Date

#### **Section 1. Authority and Purpose**

The Superintendent of Insurance has adopted this Rule, pursuant to 24-A M.R.S.A. §§ 212, 417, 6104, and 6718(2), in order to establish financial standards and corporate governance standards for domestic risk retention groups (RRGs).

#### **Section 2. Scope**

Section 3 applies to all RRGs with operations or a place of business in this State. Section 4 applies to all domestic RRGs. Section 5 applies to all domestic RRGs licensed by the Superintendent as captive insurers.

#### **Section 3 Licensure**

Any risk retention group, as defined in 24-A M.R.S.A. § 6093(13), and any entity holding itself out as a risk retention group or RRG or describing itself using substantially similar terminology, that does business or is incorporated or domiciled in this State or does business in another jurisdiction from a place of business in this State, must either:

1. Be licensed by the Superintendent as a casualty insurer pursuant to 24-A M.R.S.A. § 404 with authority to transact casualty insurance;
2. Be licensed by the Superintendent as an association or industrial insured captive insurer pursuant to 24-A M.R.S.A. § 6702 with authority to transact casualty insurance; or
3. Hold an appropriate license from its domiciliary regulator and, if doing business or holding itself out as doing business in this State, be registered with the Superintendent as a foreign RRG pursuant to 24-A M.R.S.A. § 6095.

#### **Section 4 Corporate Governance and Operational Standards for Domestic RRGs**

All RRGs domiciled and licensed in this State shall comply with the following corporate governance and operational standards.

##### **1.. *Board of Directors***

- A. The RRG's board of directors shall have a majority of independent directors. A director does not qualify as independent unless the board affirmatively determines that the director has no material relationship with the RRG. The RRG shall review its determinations of independence and disclose them to the Superintendent at least annually.
  - (1) A director has a material relationship with the RRG if the director, an immediate family member, or any business with which the director is affiliated has received compensation or other valuable consideration from the RRG or from any consultant or service provider to the RRG, during any consecutive 12-month period, beginning within the preceding 24 months, that is greater than or equal to 5% of the RRG's gross written premium or 2% of its surplus, as measured at the end of any fiscal quarter ending within that 12-month period.
  - (2) A director has a material relationship with the RRG if the director or an immediate family member is, or has been within the past year, affiliated with or employed in a professional capacity by a present or former internal or external auditor of the RRG.
  - (3) A director has a material relationship with the RRG if the director or an immediate family member is, or has been within the past year, employed as an executive officer of a business entity whose board of directors or management includes any of the RRG's current executives.
  - (4) The relationships described in Subparagraphs (1) through (3) are examples, not an exhaustive list. The board shall regard any relationship that would give a reasonable person comparable or greater concerns about the director's independence as a material relationship.

- (5) Membership in the RRG, direct or indirect ownership of a member of the RRG, or service as an employee, director, or officer of a member of the RRG or the direct or indirect parent of a member of the RRG, is not considered a material relationship with the RRG and therefore does not, without more, disqualify someone with such a relationship with a member of the RRG from serving as an independent director of the RRG.
  - (B) If an RRG is not organized as a stock or mutual insurance corporation, the term “board of directors” shall refer to its managers, subscribers’ advisory committee, or similar governing body. If an organization comprising the members of the RRG is the sole owner of the RRG and the Superintendent determines that the parent organization’s board possesses and exercises effective control over the RRG, then the board of directors of the parent organization shall be considered the board of directors of the RRG for purposes of this Section; otherwise, both boards of directors are subject to all applicable requirements of this Section.
  - (C) If the RRG is a reciprocal insurer, its attorney-in-fact shall adhere to the same standards regarding independence of operation and governance as imposed on the RRG’s subscribers’ advisory committee under this Section. The RRG’s attorney-in-fact may not:
    - (a) Contract directly, rather than on behalf of the RRG, with any service provider for services to the RRG; or
    - (b) Recruit, negotiate with, or make the decision to engage any service provider with which the attorney-in-fact has a material relationship.
2. *Service Provider Contracts.* The term of a material service provider contract with the RRG shall not exceed 5 years. Any such contract, or its renewal, shall require the approval of the majority of the RRG’s independent directors. The board shall have the right to terminate any service provider, audit, or actuarial contracts at any time for cause after providing adequate notice as reasonably defined in the contract.
- (A) Service providers include captive managers, auditors, accountants, actuaries, investment advisors, legal service providers, managing general underwriters, and any other persons or entities responsible for underwriting, determination of rates, collection of premium, adjusting and settling claims, or the preparation of financial statements.
  - (B) A service provider contract is material if the amount to be paid for the contract is greater than or equal to 5% of the RRG’s annual gross written premium or 2% of its surplus, whichever is greater.
  - (C) A lawyer retained by the RRG to defend insurance claims is not considered the RRG’s legal service provider unless the lawyer also provides other legal services to the RRG, or the lawyer has received material levels of compensation for claims defense during three of the past five calendar years.

- (D) No material service provider contract may take effect unless the RRG has notified the Superintendent in writing of its intention to enter into the contract at least one month before the requested effective date and the Superintendent has not disapproved it within the review period.
3. *Plan of Operation.* A domestic RRG offering insurance in any jurisdiction shall have in force, and shall adhere to, a plan of operation, adopted by the board and approved by the Superintendent, that includes all the elements specified in 24-A M.R.S.A. § 6093(8) and satisfies the requirements of this Subsection. The RRG shall file any material amendments or revisions to the plan of operation with the Superintendent within ten days after their adoption. The plan of operation shall obligate the board to:
- (A) Discharge its duties with the care, skill, prudence, and diligence of prudent directors acting in a similar enterprise and purpose;
  - (B) Ensure that all insured members of the RRG receive evidence of ownership interest in the RRG or its parent organization;
  - (C) Ensure that the RRG's management is accountable for the RRG's compliance with the plan of operation and with applicable law, including the obligation to write only insurance to cover liabilities, incurred by its members, of the kinds described in 24-A M.R.S.A. § 6093(6) and 15 U.S.C. § 3901(a)(2);
  - (D) Develop a set of governance standards for the RRG;
  - (E) Oversee the evaluation of the RRG's management, including but not limited to the performance of any captive manager, managing general underwriter, or other party or parties responsible for underwriting, determination of rates, collection of premium, adjusting or settling claims, or the preparation of financial statements;
  - (F) Review and approve the amount to be paid for all material service providers; and
  - (G) Review and approve, at least annually:
    - (1) The RRG's goals and objectives, its expectations for the performance of its officers and service providers in meeting those goals and objectives, and a management compensation plan consistent with those expectations;
    - (2) The officers' and service providers' performance in light of those goals and objectives; and,
    - (3) The continued retention of the officers and material service providers in light of their performance reviews.
4. *Governance Standards.* The board shall adopt and adhere to governance standards, shall post them on the RRG's website or disclose them through other means the board determines to be reasonable and effective, and shall provide copies to the RRG's members on request. The governance standards shall include:

- (A) A process by which the directors are elected by the RRG's insured members;
  - (B) Director qualification standards;
  - (C) Director responsibilities;
  - (D) Director access to management and, as necessary and appropriate, independent advisors;
  - (E) Director compensation;
  - (F) Director orientation and continuing education;
  - (G) Policies and procedures for management succession; and
  - (H) Policies and procedures for annual performance evaluation of the board.
5. *Business Conduct and Ethics.* The board shall adopt and disclose a code of business conduct and ethics for directors, officers, and employees. If the code contains any waiver provisions, any waivers that are granted shall be promptly disclosed to all directors. The code shall include the following topics:
- (A) Conflicts of interest;
  - (B) Matters covered under this State's corporate opportunities doctrine;
  - (C) Confidentiality;
  - (D) Fair dealing;
  - (E) Protection and proper use of RRG assets;
  - (F) Compliance with all applicable law; and
  - (G) Requirements to report any illegal or unethical behavior that affects the operation of the RRG.
6. *Reporting Noncompliance.* The president or chief executive officer of the RRG, and any captive manager or other service provider performing executive functions, shall promptly notify the Superintendent in writing if any of them becomes aware of any material noncompliance with the requirements of this Section or standards adopted by the RRG pursuant to this Section.
7. *Transition.* All domestic RRGs currently doing business shall come into full compliance with this Section no later than January 1, 2015, or such reasonable later date as the Superintendent may approve at the request of the RRG for good cause shown. To the extent that they attain compliance or substantial compliance with any provisions of this section before that date, they shall maintain that level of compliance for the remainder of the transition period.

## Section 5. RRGs Licensed as Captive Insurers

Notwithstanding any exemption from the requirements of the Maine Insurance Code otherwise available to captive insurers, an RRG that is licensed by the Superintendent as a captive insurer is subject to the following requirements:

1. *Examinations.* The Superintendent shall have all powers and responsibilities to examine any person with respect to the affairs and transactions of a captive RRG and, if applicable, its holding company system, as set forth in 24-A M.R.S.A. §§ 221, 222(1-A), and 223 through 228.
  - (A) Nothing in 24-A M.R.S.A. § 6708 or other provisions of the captive insurance law shall be construed as a limitation on the Superintendent's examination authority under this Subsection.
  - (B) Any examination report is a public record to the extent provided in 24-A M.R.S.A. § 227, notwithstanding 24-A M.R.S.A. § 6708(2).
2. *Accounting Practices and Procedures.* A captive RRG's assets and liabilities shall be valued and reported in accordance with statutory accounting principles as provided in 24-A M.R.S.A. § 901-A, subject to such permitted and prescribed practices as are appropriate to the nature, scope, and complexity of the RRG's business.
  - (A) A captive RRG shall be considered a domestic property and casualty insurer for purposes of the Maine Risk-Based Capital Standards Act, 24 A M.R.S.A. Chapter 79 (§§ 6451 *et seq.*), as modified by the provisions of this Paragraph.
    - (1) For purposes of provisions requiring disclosure of information to regulators in other states, a captive RRG is considered "authorized" in any state where it is registered under that state's Risk Retention Act or substantially similar law.
    - (2) A captive RRG shall not be required to disclose risk-based capital information in any state that does not provide effective confidentiality protections for such information.
    - (3) The Superintendent may grant an exemption that adjusts the action level thresholds or modifies the corrective action requirements if the captive RRG demonstrates to the satisfaction of the Superintendent that:
      - (a) All continuing members of the captive RRG have given their informed consent to the exemption, and effective measures have been taken to provide adequate protection to all departing members for their outstanding exposures, including appropriate prioritization of claims payment obligations;

- (b) Effective measures are in place for monitoring the ongoing performance of the captive RRG and promptly responding to adverse events; and
    - (c) All continuing members of the RRG are financially strong and able to withstand the risks posed by the exemption, giving due consideration to any financial guaranty given by a financially strong sponsoring organization or other financially strong guarantor. There is a rebuttable presumption that a member or guarantor that has submitted at least three years of historical audited financial statements is considered financially strong if it has an investment-grade rating from a nationally recognized statistical rating organization, or tangible net worth equal to the lesser of \$100 million or ten times the captive RRG's largest net retained per-occurrence limit.
  - (B) A captive RRG shall prepare annual financial statements and quarterly reports of financial condition in the form prescribed by the National Association of Insurance Commissioners (NAIC) and in accordance with the applicable NAIC reporting instructions and the NAIC *Accounting Practices and Procedures Manual*. They shall be filed with the Superintendent and filed electronically with the NAIC in compliance with 24-A M.R.S.A. § 423 and 423-A.
  - (C) A captive RRG shall file reports of any material transactions as provided in 24-A M.R.S.A. § 423-C, and such additional financial reports as the Superintendent may require pursuant to 24-A M.R.S.A. § 6707(4).
  - (D) A captive RRG shall be considered a domestic insurer for purposes of 24-A M.R.S.A. § 221-A and the Audited Financial Report Rule, Maine Bureau of Insurance Rule 235. The audited financial statement required by Rule 235 shall be accepted in lieu of the GAAP audit that would otherwise be required by 24-A M.R.S.A. § 6707(1). A captive RRG shall not be eligible for the small insurer exemption under 24-A M.R.S.A. § 221-A(7) except with the affirmative permission of the Superintendent.
  - (E) A captive RRG shall be considered a domestic insurer for purposes of the Maine Property and Casualty Actuarial Opinion Act, 24-A M.R.S.A. Chapter 11, Subchapter 5 (§§ 991 *et seq.*)
  - (F) Notwithstanding 24-A M.R.S.A. § 6710, any alternative valuation or rating methodology proposed by an RRG that is licensed as an association captive insurance company shall be evaluated by the Superintendent in the same manner and under the same standards as any other request for a permitted accounting practice subject to this Rule.
3. *Holding Company Systems.* A captive RRG shall be considered a domestic insurer for purposes of the Maine Insurance Holding Company System Act, 24-A M.R.S.A. § 222,

and the Holding Company Rule, Maine Bureau of Insurance Rule 180, except to the extent that the Superintendent modifies those requirements to address unique aspects of the organization and operations of RRGs.

4. *Reinsurance.* Reinsurance ceded and assumed by a captive RRG is subject to the following requirements.
  - (A) A captive RRG shall be considered a domestic insurer for purposes of the Maine Credit for Reinsurance Act, 24-A M.R.S.A. § 731-B, except that with the Superintendent's approval and subject to such terms and conditions as the Superintendent may establish for the protection of the RRG and its members, a captive RRG may take credit for reinsurance ceded to another RRG in which the RRG or the members whose exposure is reinsured are eligible for membership.
  - (B) A captive RRG shall be considered a domestic insurer for purposes of the additional standards for ceded reinsurance set forth in 24-A M.R.S.A. §§ 731-C through 731-E.
  - (C) A captive RRG may only assume reinsurance from another RRG if the other RRG or the members whose exposure is reinsured are eligible for membership in the captive RRG, and the Superintendent determines that the risks assumed are similar or related to those insured by the captive RRG and that the captive RRG can safely assume those risks.
5. *Diversification of Risk.* A captive RRG shall avoid any imprudent concentration of risk in any one subject of insurance. The Superintendent may take such remedial action as may be necessary to prevent or correct a violation of this Subsection, including ordering the RRG to deny, terminate, or reinsure any coverage creating an imprudent concentration of risk.
6. *Other Provisions Applicable.* A captive RRG shall be considered a domestic insurer for purposes of the following provisions of the Maine Insurance Code and rules adopted by the Superintendent thereunder:
  - (A) The Maine Business Transacted with Broker-Controlled Insurer Act, 24-A M.R.S.A. Chapter 77 (§§ 6401 *et seq.*);
  - (B) The Maine Managing General Agents Act, 24-A M.R.S.A. Chapter 16, Subchapter 8 (§§ 1491 *et seq.*);
  - (C) The Maine Reinsurance Intermediary Act, 24-A M.R.S.A. Chapter 9, Subchapter 4 (§§ 741 *et seq.*); and
  - (D) The Hazardous Condition Rule, Maine Bureau of Insurance Rule 710.
7. *Transparency.* To the extent that any disclosure requirement for captive RRGs, established or incorporated by reference by this Rule, conflicts with any confidentiality provision of the Maine Captive Insurance Company Act, 24-A M.R.S.A. Chapter 83, the



disclosure requirement shall control. An RRG that is licensed as an association captive insurance company shall be subject to the disclosure requirements applicable to industrial insured groups under 24-A M.R.S.A. §§ 6707 and 6715. Each captive RRG shall acknowledge in writing, when it submits its plan of operation or feasibility study under 24-A M.R.S.A. § 6094 or within 30 days after the effective date of this Rule, that as an RRG it assumes public reporting obligations not imposed on other captive insurers.

8. *Standards for Discretionary Acts.* When considering whether to grant any permitted accounting practice, or other request by a captive RRG for exemption, waiver, or modification of any requirement of general applicability, the Superintendent shall give due consideration to the lack of guaranty association protection for members insured by RRGs, and to the impact on the nationwide market in which the captive RRG is authorized by the Superintendent to do business. The Superintendent may enter into interstate regulatory cooperation agreements and arrangements to establish uniform standards and guidelines for the regulation of RRGs by their domiciliary states.

#### **Section 6. Severability**

If any section or portion of a section of this Rule or its applicability to any person or circumstance is held invalid by a court, the remainder of the Rule or the applicability of the provision to other persons or circumstances shall not be affected.

#### **Section 7. Effective date**

This Rule is effective Jul 12, 2014.